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SIGMATRON INTERNATIONAL INC

Form 10-Q

March 14, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended January 31, 2007

Commission File Number 0-23248

SigmaTron International, Inc.
(Exact Name of Registrant, as Specified in its Charter)

Delaware
(State or other Jurisdiction of
Incorporation or Organization)

36-3918470
(I.R.S. Employer
Identification Number)

2201 Landmeier Road, Elk Grove Village, Illinois 60007
(Address of Principal Executive Offices)

Registrant's Telephone Number, Including Area Code: (847) 956-8000

No Change
(Former Name, Former Address, and Former Fiscal Year,
if Changed Since Last Report)

Indicate, by check mark, whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. Large accelerated filer Accelerated filer Non-accelerated .

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act) Yes No

On March 12, 2007, there were 3,794,956 shares of the Registrant's Common Stock outstanding.

SigmaTron International, Inc.

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SIGMATRON INTERNATIONAL, INC.
Consolidated Balance Sheets

| | January 31, 2007 (Unaudited) | April 30, 2006 |
|---|------------------------------------|-------------------|
| | ----- | ----- |
| CURRENT ASSETS: | | |
| Cash | \$ 2,369,154 | \$ 3,269,925 |
| Accounts receivable, less allowance for doubtful accounts of \$268,920 at January 31, 2007 and April 30, 2006 | 21,512,929 | 17,747,414 |
| Inventories, net | 38,290,480 | 31,250,050 |

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| | | |
|---|---------------|--------------|
| Income taxes refundable | 114,776 | 476,000 |
| Prepaid and other assets | 1,565,222 | 1,329,774 |
| Deferred income taxes | 970,440 | 957,069 |
| Other receivables | 192,252 | 332,298 |
| | ----- | ----- |
| Total current assets | 65,015,253 | 55,362,530 |
| Property, machinery and equipment, net | 31,404,199 | 30,544,307 |
| Other assets | 945,196 | 1,548,240 |
| Intangible assets, net of amortization \$1,137,684 and \$583,650 | 1,632,316 | 2,186,350 |
| Goodwill | 9,298,945 | 9,298,945 |
| | ----- | ----- |
| Total assets | \$108,295,909 | \$98,940,372 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Trade accounts payable | \$ 15,714,231 | \$13,444,928 |
| Accrued expenses | 2,149,687 | 2,163,542 |
| Accrued wages | 2,318,423 | 1,743,076 |
| Income taxes payable | -- | 839,438 |
| Notes payable - bank | 750,000 | 1,000,000 |
| Notes payable - building | 522,070 | 430,000 |
| Capital lease obligations | 1,655,224 | 1,408,485 |
| | ----- | ----- |
| Total current liabilities | 23,109,635 | 21,029,469 |
| Notes payable - banks | 27,054,611 | 21,161,900 |
| Notes payable- building, less current portion | 3,122,686 | 3,591,088 |
| Capital lease obligations, less current portion | 3,560,269 | 2,804,345 |
| Deferred income taxes | 2,458,759 | 2,458,759 |
| | ----- | ----- |
| Total long-term liabilities | 36,196,325 | 30,016,092 |
| | ----- | ----- |
| Total liabilities | 59,305,960 | 51,045,561 |
| COMMITMENTS AND CONTINGENCIES: | | |
| STOCKHOLDERS' EQUITY: | | |
| Preferred stock, \$.01 par value; 500,000 shares authorized, none issued and outstanding | -- | -- |
| Common stock, \$.01 par value; 12,000,000 shares authorized, 3,794,956 and 3,786,956 shares issued and outstanding at January 31, 2007 and April 30, 2006 | 37,950 | 37,870 |
| Capital in excess of par value | 19,219,104 | 19,167,289 |
| Retained earnings | 29,732,895 | 28,689,652 |
| | ----- | ----- |
| Total stockholders' equity | 48,989,949 | 47,894,811 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$108,295,909 | \$98,940,372 |
| | ===== | ===== |

See accompanying notes to financial statements.

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| | Three Months Ended January 31, 2007 | Three Months Ended January 31, 2006 | Nine Months Ended January 31, 2006 |
|--|--|--|--|
| Net sales | \$44,584,513 | \$34,061,657 | \$126,061,657 |
| Cost of products sold | 40,281,945 | 30,381,859 | 113,061,859 |
| Gross profit | 4,302,568 | 3,679,798 | 13,000,000 |
| Selling and administrative expenses | 3,519,246 | 2,886,874 | 9,000,000 |
| Operating income | 783,322 | 792,924 | 3,000,000 |
| Other income | (59,835) | (80,927) | (1,000,000) |
| Interest expense | 717,648 | 435,888 | 1,000,000 |
| Income from continuing operations before income tax expense | 125,509 | 437,963 | 1,000,000 |
| Income tax expense | 48,937 | 150,628 | 1,000,000 |
| Income from continuing operations | 76,572 | 287,335 | 1,000,000 |
| Discontinued operations | | | |
| Gain on sale of Las Vegas operation | -- | -- | -- |
| (Loss) income from operations of discontinued Las Vegas location | -- | (15,014) | (1,000,000) |
| Income tax benefit | -- | (5,855) | (1,000,000) |
| Loss on discontinued operation | -- | (9,159) | (1,000,000) |
| Net income | \$ 76,572 | \$ 278,176 | \$ 1,000,000 |
| Earnings (loss) per share - basic | | | |
| Continuing operations | \$ 0.02 | \$ 0.08 | \$ 0.08 |
| Discontinuing operations | -- | -- | -- |
| Total | \$ 0.02 | \$ 0.08 | \$ 0.08 |
| Earnings (loss) per share - diluted | | | |
| Continuing operations | \$ 0.02 | \$ 0.07 | \$ 0.07 |
| Discontinuing operations | -- | -- | -- |
| Total | \$ 0.02 | \$ 0.07 | \$ 0.07 |
| Weighted average shares of common stock outstanding | | | |
| Basic | 3,794,956 | 3,755,420 | 3,755,420 |
| Weighted average shares of common stock outstanding | | | |
| Diluted | 3,895,939 | 4,192,229 | 3,755,420 |

See accompanying notes to financial statements

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| | January 31, 2007 | January 31, 2006 |
|--|---------------------|---------------------|
| | ----- | ----- |
| OPERATING ACTIVITIES: | | |
| Net income | \$ 1,043,252 | \$ 1,664,575 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation | 3,031,122 | 3,218,763 |
| Stock-based compensation | 34,286 | -- |
| Provision for inventory obsolescence | -- | 160,000 |
| Provision for doubtful accounts | -- | 10,000 |
| Deferred income taxes | (13,371) | (183,273) |
| Amortization of intangible assets | 554,034 | -- |
| Gain on sale of discontinued operation | -- | (310,731) |
| Changes in operating assets and liabilities, net of acquisition | | |
| Accounts receivable | (3,765,515) | 90,091 |
| Inventories | (7,040,430) | (4,208,925) |
| Prepaid expenses and other assets | 868,866 | (1,012,299) |
| Trade accounts payable | 2,269,303 | (475,014) |
| Accrued expenses and wages | 561,492 | (808,739) |
| Income taxes payable | (839,438) | 98,755 |
| | ----- | ----- |
| Net cash used in operating activities | (3,296,399) | (1,756,797) |
| INVESTING ACTIVITIES: | | |
| Acquisition of Able | -- | (16,771,755) |
| Purchases of machinery and equipment | (1,728,839) | (2,781,631) |
| Proceeds from sale of Las Vegas operation | -- | 1,705,695 |
| | ----- | ----- |
| Net cash used in investing activities | (1,728,839) | (17,847,691) |
| FINANCING ACTIVITIES: | | |
| Proceeds from issuance of common stock | 17,600 | 2,720,415 |
| Payments under capital lease obligation | (1,159,512) | (938,401) |
| Payments other notes payable | -- | (300,000) |
| Payments under term loan | (250,000) | |
| Proceeds under term loan | 1,250,000 | -- |
| Proceeds under lines of credit | 4,642,711 | 20,509,702 |
| Payments under building notes payable | (376,332) | (360,062) |
| | ----- | ----- |
| Net cash provided by financing activities | 4,124,467 | 21,631,654 |
| CHANGE IN CASH | (900,771) | 2,027,166 |
| Cash at beginning of period | 3,269,925 | 184,014 |
| | ----- | ----- |
| CASH AT END OF PERIOD | \$ 2,369,154 | \$ 2,211,180 |
| | ===== | ===== |
| Supplementary disclosures of cash flow information | | |
| Cash paid for interest | \$ 1,890,947 | \$ 886,652 |
| Cash paid for income taxes, net of (refunds) | 1,415,033 | 796,827 |

See accompanying notes to financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

January 31, 2007

NOTE A - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of SigmaTron International, Inc. ("SigmaTron"), its wholly owned subsidiaries Standard Components de Mexico S.A., Ablemex, S.A. de C.V., acquired in July 2005, and its wholly-owned foreign enterprise Wujiang SigmaTron Electronics Co. Ltd. ("SigmaTron China"), and its procurement branch SigmaTron Taiwan (collectively, the "Company"), have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X.

Accordingly, the consolidated financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three and nine month periods ended January 31, 2007, are not necessarily indicative of the results that may be expected for the year ending April 30, 2007. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended April 30, 2006.

NOTE B - INVENTORIES

The components of inventory consist of the following:

| | January 31, 2007 | April 30, 2006 |
|-------------------|---------------------|-------------------|
| Finished products | \$ 8,959,564 | \$ 8,216,317 |
| Work-in-process | 3,687,303 | 2,563,334 |
| Raw materials | 25,643,613 | 20,470,399 |
| | ----- | ----- |
| | \$38,290,480 | \$31,250,050 |
| | ===== | ===== |

NOTE C - STOCK INCENTIVE PLANS

The Company adopted Financial Accounting Standards Board, Share-Based Payment ("SFAS 123(R)") on May 1, 2006, and implemented the new standard utilizing the modified prospective application transition method. SFAS 123(R) requires the Company to measure the cost of employee services received in exchange for an equity award based on the grant date fair value. Compensation expense for which the requisite service requirement that has not been rendered and are outstanding as of the option grant date will be recognized over the remaining service period. In July 2006, the Company granted 10,000 options to a non-executive employee and the per share fair value of the options granted was \$6.0125. The Company recognized approximately \$20,000 in stock compensation expense associated with the grant and a tax benefit of approximately \$7,800 as of

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October 31, 2006. In the third quarter of fiscal 2007, the Company granted 6,000 options to non-executive employees and the fair value of the option grants were \$6.57 and \$7.23. The Company recognized approximately \$14,245 in stock compensation expense associated with the grants and a tax benefit of approximately \$5,550 as of January 31, 2007.

Under the Company's stock option plans, options to acquire shares of common stock have been made available for grant to certain employees and directors. Each option granted has an exercise price of not less than 100% of the market value of the common stock on the date of grant. The contractual life of each option is generally 10 years. The vesting of the grants varies according to the individual options granted.

Prior to the adoption of SFAS 123(R), the Company had elected to apply Accounting Principles Board Opinion 25 to account for its stock-based compensation plans, as permitted under SFAS No. 123, Accounting for Stock-Based Compensation. This method applied the intrinsic value method for stock options and other awards granted to employees. Had the fair value method been used during the three and nine months ended January 31, 2006, the following pro forma net income would be as reported:

| | Three Months Ended January 31, 2006 | Nine Months Ended January 31, 2006 |
|---|---|--|
| | ----- | ----- |
| Net Income, as reported | \$ 278,176 | \$1,664,575 |
| Deduct: total stock-based employee compensation expense determined under fair based method for awards granted, modified, or settled, net of related tax effects | (291,206) | (873,617) |
| | ----- | ----- |
| Pro forma net income | \$ (13,030) | \$ 790,958 |
| | ===== | ===== |

| | Three Months Ended January 31, 2006 | Nine Months Ended January 31, 2006 |
|-----------------------|---|--|
| | ----- | ----- |
| Earnings per share | | |
| Basic - as reported | \$.08 | \$.45 |
| Basic - pro forma | (.01) | .21 |
| | ===== | ===== |
| Diluted - as reported | .07 | .40 |
| Diluted - pro forma | \$ (.01) | \$.19 |
| | ===== | ===== |

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The fair value of each option grant is estimated on the grant date using the Black-Scholes option pricing model with the following assumptions:

| | Nine Months Ended | |
|---|---------------------|---------------------|
| | January 31, 2007 | January 31, 2006 |
| Expected dividend yield | .0% | 0% |
| Expected stock price volatility | .750 | .800 |
| Average risk-free interest rate | 4.98% | 2.20% |
| Weighted-average expected life of options | 6.5 years | 5 years |

Option-valuation models require the input of highly subjective assumptions. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion the existing method does not necessarily provide a reliable single measure of the fair value of the Company's employee stock options. There were 6,000 stock options granted in the third quarter ended January 31, 2007.

The table below summarizes option activity from the beginning of fiscal year 2007 through January 31, 2007:

| | Number of options | Range of exercise prices | | Weighted average exercise price |
|---|----------------------|-----------------------------|---------|---------------------------------------|
| | | Low | High | |
| Options outstanding at May 1, 2006 | 523,307 | \$2.20 | \$12.25 | \$7.87 |
| Options granted | 16,000 | 9.17 | 10.12 | 9.47 |
| Exercised | (8,000) | 2.20 | 2.20 | 2.20 |
| Options outstanding at January 31, 2007 | 531,307 | \$2.20 | \$12.25 | \$8.00 |

As of January 31, 2007, there was approximately \$68,570 of unrecognized compensation cost related to nonvested share-based compensation arrangements, which is expected to be recognized over an average period of 2.67 years.

Information with respect to stock options outstanding and stock options exercisable at January 31, 2007, follows:

| Range of exercise prices | Options Outstanding | | |
|--------------------------|--|---|--|
| | Number outstanding at January 31, 2007 | Weighted-average remaining contractual life | Weighted- average exercise price |
| \$2.20 - 5.63 | 103,515 | 4.65 years | \$2.51 |

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| | | | |
|--------------|---------|------------|--------|
| 9.17 - 12.25 | 427,792 | 8.06 years | \$9.33 |
| | ----- | | |
| Total | 531,307 | | |
| | ===== | | |

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| Options Exercisable | | |
|--------------------------|--|--|
| Range of exercise prices | Number exercisable at January 31, 2007 | Weighted- average exercise price |
| ----- | ----- | ----- |
| \$2.20 - 5.63 | 103,515 | \$2.51 |
| 9.17 - 12.25 | 399,186 | \$9.33 |
| | ----- | |
| Total | 502,701 | |
| | ===== | |

NOTE D - STRATEGIC TRANSACTION

In July 2005, the Company closed on the purchase of all of the outstanding common stock of Able Electronics Corporation ("Able"), a company headquartered in Hayward California, and its wholly owned subsidiary, Ablemex S.A. de C.V., located in Tijuana, Mexico. Able was an ISO 9001:2000 certified EMS company serving Original Equipment Manufacturers in the life sciences, telecommunications and industrial electronics industries. The acquisition of Able has allowed the Company to make strides towards achieving four objectives: (1) to further diversify its markets, capabilities and customer base, (2) adding a third low-cost manufacturing facility in Tijuana, Mexico, (3) creating an opportunity to consolidate the California operations into one facility, and (4) to generate incremental revenue from Able's customers as they become familiar with the Company's broader array of services. The effective date of the transaction was July 1, 2005. Able was merged into the Company beginning November 1, 2005 and operates as a division of the Company. The purchase price was approximately \$16,800,000 and was recorded as a stock purchase transaction in the first quarter of fiscal year 2006. The transaction was financed by the Company's amended credit facility and resulted in an increase of approximately \$8,500,000 in goodwill. Assuming the purchase was recorded as of the first period reported, May 1, 2005, unaudited revenues for the three and nine months ended January 31, 2006, would have been \$24,576,808 and \$93,531,730, respectively. The unaudited pro-forma dilutive earnings per share for the three and nine month period ended January 31, 2006, would have been (\$.27) and \$.13, respectively.

NOTE E - DISCONTINUED OPERATIONS

In June 2005, the Company closed on the sale of its Las Vegas, Nevada operation. The Las Vegas facility operated as a complete EMS center specializing in the assembly of electronic products and cables for a broad range of customers primarily in the gaming industry. The effective date of the transaction was May 30, 2005. The transaction was structured as an asset sale, and included a \$2,000,000 cash payment to the Company for the buyer's purchase of the machinery, equipment and other assets of the Las Vegas operation. The

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transaction was recorded by the Company in the first quarter of fiscal year 2006 and included a gain on the transaction of approximately \$311,000. The gain was offset by a loss of approximately \$383,000 on discontinued operations for the Las Vegas operation for the period ended April 30, 2006. A net loss of approximately \$9,000 and \$36,000 was recorded in the three and nine months ended January 31, 2006, respectively.

NOTE F - FINANCING TRANSACTION

The Company entered into an Amended Loan and Security Agreement in July 2005, which provided for a revolving credit facility. The maximum borrowing limit under the amended revolving credit

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facility is limited to the lesser of: (i) \$17,000,000 or (ii) an amount equal to the sum of 85% of the receivable borrowing base and the lesser of \$8,500,000 or a percentage of the inventory base. The Amended Loan and Security Agreement expires on June 30, 2008 and includes certain financial covenants. The Amended Loan and Security Agreement also includes a four year term loan in the amount of \$3,000,000.

On July 31, 2006, the Company amended the credit facility to increase the revolving credit facility from \$22,000,000 to \$27,000,000. The amended revolving credit facility is limited to the lesser of: (i) \$27,000,000 or (ii) an amount equal to the sum of 85% of the receivable borrowing base and the lesser of \$13,500,000 or a percentage of the inventory base. The revolving credit facility expires June 30, 2009. The term loan was increased to \$4,000,000 from \$2,750,000. Interest payments only are due through June 30, 2007 and quarterly principal payments of \$250,000 are due each quarter beginning with the quarter ending June 30, 2007, through the quarter ending June 30, 2011. In October 2006, the Company further amended the credit facility to increase the revolving credit facility from \$27,000,000 to \$32,000,000. The increase of \$5,000,000 is for a term of six months. At January 31, 2007, the Company was in compliance with its financial covenants and in the third quarter of fiscal year 2007 the interest coverage covenant was amended. At January 31, 2007 \$27,804,611 was outstanding under the revolving credit facility and term loan. There was approximately \$3,158,000 of unused credit available as of January 31, 2007.

The loan and security agreement is collateralized by substantially all of the domestically-located assets of the Company and contains certain financial covenants, including specific covenants pertaining to the maintenance of minimum tangible net worth and net income. The agreement also restricts annual lease rentals and capital expenditures and the payment of dividends.

CRITICAL ACCOUNTING POLICIES:

Management Estimates and Uncertainties - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates made in preparing the consolidated financial statements include depreciation and amortization periods, the allowance for doubtful accounts, reserves for inventory and valuation of goodwill. Actual results could materially differ from these estimates.

Revenue Recognition - Revenues from sales of product including the Company's

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electronic manufacturing services business are recognized when the product is shipped to the customer. In general, it is the Company's policy to recognize revenue and related costs when the order has been shipped from our facilities, which is also the same point that title passes under the terms of the purchase order except for consignment inventory. Consignment inventory is shipped from the Company to an independent warehouse for storage or shipped directly to the customer and stored in a segregated part of the customer's own facility. Upon the customer's request for inventory, the consignment inventory is shipped to the customer if the inventory was stored offsite or transferred from the segregated part of the customer's facility for consumption, or use, by the customer. The Company recognizes revenue upon such transfer. The Company does not earn a fee for storing the consignment inventory. The Company provides a ninety (90) day warranty for workmanship only and does not have any installation, acceptance or sales incentives, although the Company has negotiated extended warranty terms in certain instances. The Company assembles and tests assemblies based on customers' specifications. Historically, the amount of returns for workmanship issues has been de

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minus under the Company's standard or extended warranties. Any returns for workmanship issues received after each period end are accrued in the respective financial statements.

Inventories - Inventories are valued at the lower of cost or market. Cost is determined by the first-in, first-out method. The Company establishes inventory reserves for valuation, shrinkage, and excess and obsolete inventory. The Company records provisions for inventory shrinkage based on historical experience to account for unmeasured usage or loss. Actual results differing from these estimates could significantly affect the Company's inventories and cost of products sold. The Company records provisions for excess and obsolete inventories for the difference between the cost of inventory and its estimated realizable value based on assumptions about future product demand and market conditions. Actual product demand or market conditions could be different than that projected by management.

Impairment of Long-Lived Assets - The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An asset is considered impaired if its carrying amount exceeds the future net cash flow the asset is expected to generate. If such asset is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset, if any, exceeds its fair market value. The Company has adopted SFAS No. 144, which establishes a single accounting model for the impairment or disposal of long-lived assets, including discontinued operations.

Goodwill and Other Intangibles - The Company adopted on June 1, 2001, SFAS No. 141 "Business Combinations". Under SFAS No. 141, a purchaser must allocate the total consideration paid in a business combination to the acquired tangible and intangible assets based on their fair value. The Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets" effective January 1, 2002. Goodwill represents the purchase price in excess of the fair value of assets acquired in business combinations. Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets", requires the Company to assess goodwill for impairment at least annually in the absence of an indicator of possible impairment and immediately upon an indicator of possible impairment. During the fourth quarter of fiscal 2006 the Company completed its annual assessment of impairment regarding the goodwill recorded. That assessment, supported by independent appraisals, did not identify any impairment as of April

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30, 2006.

NEW ACCOUNTING STANDARDS:

In June 2006, FASB Interpretation 48 ("FASB 48") "Accounting for Uncertainty in Income Taxes" was issued, which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FASB 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FASB 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition.

FASB 48 is effective for fiscal years beginning after December 15, 2006, and earlier application of the provisions of FASB 48 is encouraged if the enterprise has not yet issued financial statements, including interim financial statements, in the period that FASB 48 is adopted. The Company has not yet determined the impact of FASB 48 on its financial statements.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

NOTE: This quarterly report contains forward-looking statements. Words such as "continue," "will," "expects," "believe," "plans," and similar expressions identify forward-looking statements. These forward-looking statements are based on the current expectations of SigmaTron (including its subsidiaries). Because these forward-looking statements involve risks and uncertainties, the Company's plans, actions and actual results could differ materially. Such statements should be evaluated in the context of the risks and uncertainties inherent in the Company's business including our continued dependence on certain significant customers; the continued market acceptance of products and services offered by the Company and its customers; pricing pressures from our customers, suppliers and the market; the activities of competitors, some of which may have greater financial or other resources than the Company; the variability of our operating results; the variability of our customers' requirements; the availability and cost of necessary components and materials; the Company's ability to continue to produce products that are in compliance with the European Standard of "Restriction of Use of Hazardous Substance ("RoHS"); the ability of the Company and our customers to keep current with technological changes within our industries; regulatory compliance; the continued availability and sufficiency of our credit arrangements; changes in U.S., Mexican, Chinese or Taiwanese regulations affecting the Company's business; the continued stability of the U.S., Mexican, Chinese and Taiwanese economic systems, labor and political conditions; and the ability of the Company to manage its growth, including its expansion into China and its integration of the Able operation acquired in July 2005. These and other factors which may affect the Company's future business and results of operations are identified throughout the Company's Annual Report on Form 10-K and risk factors and may be detailed from time to time in the Company's filings with the Securities and Exchange Commission. These statements speak as of the date of this report and the Company undertakes no obligation to update such statements in light of future events or otherwise.

OVERVIEW:

The Company operates in one business segment as an independent provider of electronic manufacturing services ("EMS"), which includes printed circuit board

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assemblies and completely assembled (box-build) electronic products. In connection with the production of assembled products, the Company also provides services to its customers, including (1) automatic and manual assembly and testing of products; (2) material sourcing and procurement; (3) design, manufacturing and test engineering support; (4) warehousing and shipment services; and (5) assistance in obtaining product approval from governmental and other regulatory bodies. The Company provides these manufacturing services through an international network of facilities located in the United States, Mexico, China and Taiwan.

As the demand for electronic products has continued to increase over the past months, the lead-time for many components has increased. Pricing for some components and related commodities has escalated due to the increased demand and the transition to European Union Restriction of Use of Hazardous Substances, ("RoHS") components and may continue to increase in future periods. The impact of these price increases could have a negative effect on the Company's gross margins and operating results.

The Company relies on numerous third-party suppliers for components used in the Company's production process. Certain of these components are available only from single sources or a limited number of suppliers. In addition, a customer's specifications may require the Company to obtain components from a single source or a small number of suppliers. The loss of any such suppliers could

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have a material impact on the Company's results of operations, and the Company may be required to operate at a cost disadvantage compared to competitors who have greater direct buying power from suppliers. The Company does not enter into purchase agreements with major or single-source suppliers. The Company believes that ad-hoc negotiations with its suppliers provides flexibility, given that the Company's orders are based on the needs of its customers, which constantly change.

The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley"), as well as rules subsequently implemented by the Securities and Exchange Commission and listing requirements subsequently adopted by Nasdaq in response to Sarbanes-Oxley, have required changes in corporate governance practices, internal control policies and audit committee practices of public companies. These rules, regulations, and requirements have increased the company's legal expenses, financial compliance and administrative costs, made many other activities more time consuming and costly and diverted the attention of senior management. These rules and regulations could also make it more difficult for us to attract and retain qualified members for our board of directors, particularly to serve on our audit committee. In addition, if the Company receives a qualified opinion on the adequacy of its internal control over financial reporting, shareholders could lose confidence in the reliability of the Company's financial statements, which could have a material adverse impact on the value of the Company's stock.

Sales can be a misleading indicator of the Company's financial performance. Sales levels can vary considerably among customers and products depending on the type of services (consignment and turnkey) rendered by the Company and the demand by customers. Consignment orders require the Company to perform manufacturing services on components and other materials supplied by a customer, and the Company charges only for its labor, overhead and manufacturing costs, plus a profit. In the case of turnkey orders, the Company provides, in addition to manufacturing services, the components and other materials used in assembly. Turnkey contracts, in general, have a higher dollar volume of sales for each given assembly, owing to inclusion of the cost of components and other materials

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in net sales and cost of goods sold. Variations in the number of turnkey orders compared to consignment orders can lead to significant fluctuations in the Company's revenue levels. However, the Company does not believe that such variations are a meaningful indicator of the Company's gross margins. Consignment orders accounted for less than 5% of the Company's revenues for the period ended January 31, 2007.

In the past, the timing and rescheduling of orders have caused the Company to experience significant quarterly fluctuations in its revenues and earnings, and the Company expects such fluctuations to continue. The Company has recently experienced a general softening in customer demand across many of the markets it serves. The softening has not been significant, but may effect the fourth quarter of fiscal year 2007.

RESULTS OF OPERATIONS:

Net Sales

Net sales increased for the three month period ended January 31, 2007 to \$44,584,513 from \$34,061,657 for the three month period ended January 31, 2006. Net sales for the nine months ended January 31, 2007 increased to \$126,403,040 from \$90,267,615 for the same period in the prior fiscal year. Sales volume increased for the three and nine month periods ended January 31, 2007 as compared to the same periods in the prior year in the appliance, fitness, gaming, industrial and life sciences marketplaces. The increase in sales volume in the industrial and life sciences industries to customers is the result of the July 1, 2005 acquisition of Able.

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Gross Profit

Gross profit increased during the three month period ended January 31, 2007 to \$4,302,568 or 9.6% of net sales, compared to \$3,679,798 or 10.8% of net sales for the same period in the prior fiscal year. Gross profit increased for the nine month period ended January 31, 2007 to \$13,017,267 or 10.3% of net sales, compared to \$ 11,240,428 or 12.5% of net sales for the same period in the prior fiscal year. The decrease in the Company's gross margin as a percent of sales for the three and nine month periods is the result of pricing pressures within the EMS industry, increasing raw material costs driven primarily by increases in commodities such as copper and oil and inefficiencies at its Hayward and Tijuana operations. The Company is focused on correcting the problems at Hayward and Tijuana and is slowly making progress. In addition, the Company has expanded its Tijuana manufacturing operation and has transferred production from Hayward to Tijuana. There can be no assurance that gross margins will not continue to decrease in future quarters.

Selling and Administrative Expenses

Selling and administrative expenses increased to \$3,519,246 or 7.9% of net sales for the three month period ended January 31, 2007 compared to \$2,886,874 or 8.5% of net sales in the same period last year. Selling and administrative expenses increased to \$9,635,932 or 7.6% of net sales for the nine month period ended January 31, 2007 compared to \$7,970,016 or 8.8% of net sales in the same period last year. The increase for the three and nine month periods ended January 31, 2007, is primarily due to an increase in sales and purchasing salary expenses, commissions, accounting and legal fees, IT salaries and an increase in variable compensation. Selling and administrative expenses decreased as a percentage of net sales for the three month and nine month periods ended January 31, 2007, due to the increase in sales volume.

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Interest Expense

Interest expense for bank debt and capital lease obligations for the three month period ended January 31, 2007 was \$717,648 compared to \$435,888 for the same period in the prior year. Interest expense increased to \$1,879,688 for the nine month period ended January 31, 2007 as compared to \$935,718 for the same period in the prior year. This change was attributable to the Company's significant increased borrowings under its revolving credit facility and term loan, increased capital lease obligations and higher interest rates. The additional working capital was necessary to support the increase in sales volume.

Taxes

The effective tax rate from continuing operations for the three and nine month periods ended January 31, 2007 was 39.0%. The effective tax rate for the comparable periods in fiscal 2006 was 34.4% and 31.8% for the three and nine month periods ended, respectively. The effective tax rate in fiscal 2007 has increased compared to prior periods due to the tax effects of the Company's foreign operations.

In June 2005, the Company closed on the sale of its Las Vegas, Nevada operation. The Las Vegas facility operated as a complete EMS center specializing in the assembly of electronic products and cables for a broad range of customers primarily in the gaming industry. The effective date of the transaction was May 30, 2005. The transaction was structured as an asset sale, and included a \$2,000,000 cash payment to the Company for the buyer's purchase of the machinery, equipment and other assets of the Las Vegas operation. The transaction was recorded by the Company in the first quarter of fiscal year 2006 and included a gain on the transaction of approximately \$311,000. The

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gain was offset by a loss of approximately \$383,000 on discontinued operations for the Las Vegas operation for the period ended April 30, 2006. A net loss of approximately \$9,000 and \$36,000 was recorded in the three and nine months ended January 31, 2006, respectively.

Net Income

Net income from continuing operations decreased to \$76,572 for the three month period ended January 31, 2007 compared to \$278,176 for the same period in the prior year. Basic and diluted earnings per share for the third fiscal quarter of 2007 were \$0.02, compared to basic and diluted earnings per share of \$0.08 and \$0.07, respectively, for the same period in the prior year. For the nine months ended January 31, 2007, the Company recorded net income from continuing operations of \$1,043,252 compared to \$1,701,026 for the same period in the prior fiscal year. Basic and diluted earnings per share for the nine month period ended January 31, 2007 were \$0.28 and \$0.27 respectively, compared to basic and dilutive earnings per share of \$0.44 and \$0.40, respectively, for the same period in the prior year.

LIQUIDITY AND CAPITAL RESOURCES:

OPERATING ACTIVITIES.

Cash flow used in operating activities was \$3,296,399 for the nine months ended January 31, 2007, compared to \$1,756,797 for the prior fiscal year. During the first nine months of fiscal year 2007, cash used in operations was due to an

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increase in accounts receivable and inventory. The increase in accounts receivable is due to the increase in sales volume. The increase in inventory is primarily attributable to an increase in customer orders and the addition of RoHS compliant inventory. Cash used in operating activities was partially offset by net income, the non-cash effect of depreciation and amortization and an increase in trade payables.

INVESTING ACTIVITIES.

In June 2005, the Company closed on the sale of its Las Vegas, Nevada operation. The Las Vegas facility operated as a complete EMS center specializing in the assembly of electronic products and cables for a broad range of customers primarily in the gaming industry. The effective date of the transaction was May 30, 2005. The transaction was structured as an asset sale, and included a \$2,000,000 cash payment to the Company for the buyer's purchase of the machinery, equipment and other assets of the Las Vegas operation. The transaction was recorded by the Company in the first quarter of fiscal year 2006 and included a gain on the transaction of approximately \$311,000.

In July 2005, the Company closed on the purchase of all of the outstanding stock of Able, a company headquartered in Hayward, California and its wholly owned subsidiary, Ablemex S.A. de C.V., located in Tijuana, Mexico. Able was merged into the Company in November 2005 and currently operates as a division of the Company. The purchase price was approximately \$16,800,000 and was recorded as a stock purchase transaction in the first quarter of fiscal year 2006. The transaction was financed by the Company's amended credit facility and resulted in an increase of approximately \$8,500,000 in goodwill.

During the first nine months of fiscal 2007, the Company purchased approximately \$3,890,000 in machinery and equipment to be used in the ordinary course of business.

FINANCING TRANSACTIONS.

The Company entered into an Amended Loan and Security Agreement in July 2005, which provided for a revolving credit facility. The maximum borrowing limit under the amended revolving credit facility is limited to the lesser of: (i) \$17,000,000 or (ii) an amount equal to the sum of 85% of the receivable borrowing base and the lesser of \$8,500,000 or a percentage of the inventory base. The Amended Loan and Security Agreement expires on June 30, 2008 and includes certain financial covenants. The Amended Loan and Security Agreement also includes a four year term loan in the amount of \$3,000,000.

On July 31, 2006, the Company amended the credit facility to increase the revolving credit facility from \$22,000,000 to \$27,000,000. The amended revolving credit facility is limited to the lesser of: (i) \$27,000,000 or (ii) an amount equal to the sum of 85% of the receivable borrowing base and the lesser of \$13,500,000 or a percentage of the inventory base. The revolving credit facility expires June 30, 2009. The term loan was increased to \$4,000,000 from \$2,750,000. Interest payments only are due through June 30, 2007 and quarterly principal payments of \$250,000 are due each quarter beginning with the quarter ending June 30, 2007, through the quarter ending June 30, 2011. In October 2006, the Company further amended the credit facility to increase the revolving credit facility from \$27,000,000 to \$32,000,000. The increase of \$5,000,000 is for a term of six months. At January 31, 2007, the Company was in compliance with its financial covenants and in the third quarter of fiscal year 2007 the interest coverage covenant was amended. At January 31, 2007 \$27,804,611 was outstanding

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under the revolving credit facility and term loan. There was approximately \$3,158,000 of unused credit available as of January 31, 2007.

The loan and security agreement is collateralized by substantially all of the domestically-located assets of the Company and contains certain financial covenants, including specific covenants pertaining to the maintenance of minimum tangible net worth and net income. The agreement also restricts annual lease rentals and capital expenditures and the payment of dividends.

SigmaTron China entered into a loan agreement in April 2005, which provides for a line of credit from the China Construction Bank. The interest rate under the agreement was 5.76% and at April 30, 2006, \$1,237,500 was outstanding under the line of credit. The line of credit is collateralized by the Company's building in Suzhou-Wujiang, China and 60 of the 100 Chinese acres leased at the property. The loan was paid in full in July 2006.

The Company anticipates its credit facilities, cash flow from operations and leasing resources will be adequate to meet its working capital requirements in fiscal year 2007. In the event the business grows rapidly or the Company considers an acquisition, additional financing resources could be necessary in the current or future fiscal years. There is no assurance that the Company will be able to obtain equity or debt financing at acceptable terms in the future.

The Company provides funds for salaries, wages, overhead and capital expenditure items as necessary to operate its wholly-owned Mexican and Chinese subsidiaries. The Company provides funding to its Mexican and Chinese subsidiaries in U.S. dollars, which are exchanged for pesos and RMB as needed. The fluctuation of currencies from time to time, without an equal or greater increase in inflation, has not had a material impact on the financial results of the Company. During the first nine months of fiscal year 2007 the Company paid approximately \$15,374,000 to its subsidiaries for services provided.

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In May 2002, the Company acquired a plant in Acuna, Mexico through seller financing. The loan of \$1,950,000 is payable in equal monthly installments of approximately \$31,000 over six and a half years at a rate of 7% interest per annum. Prior to acquiring that plant, the Company rented the facility. At January 31, 2007, approximately \$614,750 was outstanding in connection with the financing of that facility.

OFF-BALANCE SHEET TRANSACTIONS:

The Company has no off-balance sheet transactions.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS:

Not applicable.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

INTEREST RATE RISK

The Company's exposure to market risk for changes in interest rates is due primarily to its short-term investments and borrowings under its credit agreements. The Company's borrowings are at a variable rate and an increase in interest rates of 1% would have resulted in interest expense increasing by approximately \$208,500 for the nine month period ended January 31, 2007. As of January 31, 2007, the Company had no short-term investments and approximately

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\$27,800,000 of borrowings under its credit agreements. The Company does not use derivative financial investments. The Company's cash equivalents, if any, are invested in overnight commercial paper. The Company does not have any significant cash flow exposure due to rate changes for its cash equivalents, because these instruments are short-term.

ITEM 4. CONTROLS AND PROCEDURES.

Our management, including our President and Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of January 31, 2007. Our disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports filed by the Company under the Securities Exchange Act of 1934 (the "Exchange Act") is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our President and Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based on this evaluation, our President and Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of January 31, 2007.

There has been no change in our internal control over financial reporting during the quarter ended January 31, 2007, that has materially affected or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

The Company is party to routine legal proceedings arising out of the normal course of business. Although it is not possible to predict with certainty the outcome of these unresolved legal actions or the range of possible loss, the Company believes that none of these actions, individually or in the aggregate, will have a material adverse effect on our financial condition or results of operations.

ITEM 1A. RISK FACTORS.

There were no material changes from our risk factors as presented in the section entitled "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended April 30, 2006 as filed with the SEC on July 28, 2006.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

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Officer and Principal Accounting
Officer)